Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of:	)	
	)	
Implementation of the Local Competition	)	CC Docket No. 96-98
Provisions in the Telecommunications	)	
Act of 1996	)	

Reply Comments of the Competition Policy Institute

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Reply Comments of the Competition Policy Institute

CC Docket No. 96-98

I. Introduction and Summary

The Competition Policy Institute ("CPI") submits these Reply Comments in the Matter of the Implementation of the Local Competition Provisions in the Telecommunications Act of 1996 ("Interconnection Rule"). CPI is a non-profit organization that advocates state and federal regulatory policies to bring competition to energy and telecommunications markets in ways that benefit consumers. We appreciate the opportunity to reply to the comments of other parties that addressed the Commission's proposed Interconnection Rule.

In these Reply Comments, we reiterate our view that the public interest is best served by a national regulatory policy framework that leads to rapid growth in local exchange service competition. The fundamental change in national telecommunications policy signaled by passage of the Telecommunications Act of 1996 cannot be overstated. Local exchange competition will do for consumers what regulation cannot fully achieve: create new products and choices for consumers and constrain consumer prices for those services. To realize the promise of this new economic and social paradigm, state and federal regulators must take affirmative steps to ensure the success of competition in local markets. Unless this new regime of local competition is encouraged to develop, consumers will be denied the main benefits of the Act.

Some commenters questioned the fundamental approach tentatively adopted by the Commission in this docket. Instead of agreeing that the Commission has a central and early role in development, some commenters would limit severely the prerogatives and responsibilities of the Commission. These parties would relegate nearly the entire responsibility for opening the local exchange to the voluntary negotiations among carriers. Our view is that this will delay implementation of local competition. Instead of getting off to a fast start, competition will have to overcome the inertia of the large incumbent LECs, and would develop largely on their schedule. In the meantime, the ILECs would undoubtedly pursue their agenda of lessened regulation at the state and federal levels. This outcome would be the most dangerous of all for consumers: reliance on competition when there is none and deregulation before market forces have developed sufficiently to control prices.

Thus we arrive at an obvious truth: in order to encourage competition sufficient to allow deregulation, regulators must act decisively at this stage to put the predicates in place. This means that the Commission and the States must adopt detailed and specific policies to implement local competition. The Telecommunications Act of 1996 might have become law on February 8, 1996, but the local exchange did not become competitive on that date.

We also agree with the CompTel that rules can be pro-competitive and deregulatory:

> The FCC correctly recognizes that adopting explicit national rules to implement Section 251 is essential to securing Congress' objective of a more competitive and deregulatory telecommunications industry. Explicit national rules will remove harmful uncertainty over how the 1996 Act will apply on a going-forward basis, while establishing the uniformity necessary to promote new entry, facilitate

> negotiations with ILECs, provide guidance to carriers and state commissions for the arbitration and review process, and limit the opportunities for the ILECs to drag their feet in implementing the core provisions in Sections 251 and 252.[1]

Contrary to the rhetoric of some of the incumbent LECs in this Docket, the Commission is not proposing excessive regulation to establish the predicates for local competition. Rather, the Commission knows that regulators must be activist and resolute to ensure that the formula established by Congress actually results in robust local competition.

After reviewing the Comments in this docket, CPI wishes to reply to comments in five areas:

- **National Rules and Regulatory Activism**

The Commission's general orientation is correct: local competition will be aided by regulatory activism; the speed with which local competition develops will be directly affected by the adoption of specific rules by the Commission and their implementation by the States.

- **Roles of the FCC and the States**

Successful implementation of the 1996 Act requires substantial effort at both state and national levels. The Commission must act to maximize jointly the activities of state and federal regulators. The States must agree that a national model for the essential ingredients (pricing and availability) is needed.

- **Unbundling and the Pricing Standards for Interconnection and Network Elements**

The Commission is correct in its tentative conclusion that TSLRIC is the appropriate standard for pricing unbundled network elements. The Commission should reject arguments from ILECs to base prices on historic costs. The Commission should liberally interpret the unbundling requirements so as to enhance the development of local competition.

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[1]Comments of CompTel at 10.

- **The Use of Bill and Keep Arrangements in Traffic Termination**

The Commission should find that States may impose bill and keep arrangements in the arbitration of interconnection negotiations.

- **Standards and Status of Arbitration by the State Commissions**

State and federal arbitration decisions are binding on the parties unless they mutually agree to renegotiate an agreement. States and the Commission should not close arbitration proceedings to parties with a legitimate interest in the outcome.

II. The Commission Should Adopt Rules Which Carry Out Congressional Intent By Encouraging Competition to Develop Quickly. The Commission Should Reject Arguments From Incumbent LECs That Competition Will Develop Without Strong Regulatory Direction

An important issue raised by the Commission in the Notice is the threshold question of how active the Commission and States should be in adopting regulations to implement the 1996 Act. Repeatedly in the Notice, the Commission discusses the need for regulations to effect a balance among the negotiators, to prevent anti-competitive pricing, to ensure that new entrants are able to assemble networks, etc. The Commission rightly saw that the growth of competition might be stunted without the active involvement of regulators at the beginning of this new enterprise. This issue was addressed directly or indirectly by most commenters, with a wide variety of responses.

The LECs tended to answer the question by assuming that barriers to the development of local competition would melt away from the heat generated in the negotiations on interconnection. SBC Communications, Inc. recommends that the FCC engage in a kinder, gentler sort of

regulation which SBC dubs "facilitative" regulation.[2] USWest advocates a "moderate" role for the Commission and then advises that the FCC should limit its involvement at the beginning of this process:

> "States do not need dictated interconnection points, network elements or pricing standards. Competition will evolve fairly if the Commission avoids overly intrusive tinkering and the states do not create a competitive landscape which favors one competitor over another."[3]

In its Comments, BellSouth reflected the view of many LECs that the Commission's role should be very proscribed and described the Commission's role as one of "support."[4] The Company suggests, as did other LEC commenters, that activism on the part of the FCC conflicted with the goals and purpose of the 1996 Act.

> The Commission's current track of pursuing and imposing detailed uniform national standards conflicts with the primary goals and purposes of the 1996 Act; to increase competition and reduce regulatory burdens. BellSouth believes that the Commission should adopt explicit national rules only in those situations where a uniform, national approach is absolutely essential to the development of competition. Thus, the scope of the Commission's regulations should be as narrow as the circumstances permit and should not interfere with the carrier-to-carrier negotiation process created under the Act.[5]

On the other hand, new entrants such as large IXCs, CAPs, cable companies, and small IXCs uniformly insisted that the strength of the incumbent LECs may well stymie attempts to achieve competition in local markets. They argue that it is essential for the Commission to mitigate the

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[2]Comments of SBC Communications at page i.

[3]Comments of USWest at 5. Footnote omitted and emphasis added.

[4]Comments of BellSouth at 3.

[5]Comments of BellSouth at page i.

strength of the ILECs by adopting and enforcing rules. The positions of the new entrants is born of experience in state commission proceedings over the past years in attempting to gain expanded interconnection. The anecdotes are depressingly similar to each other with the common feature that unbundling and access to network functions become hostage to delaying tactics, interminable negotiations, withdrawn offers, etc.

To illustrate this point, MCI related the "typical" course of negotiating with an ILEC over the unbundling of network elements.

> This is the way the typical loop unbundling implementation process has progressed in the states to date:
>
> - A State Commission orders unbundling
> - The ILEC files "compliance tariffs" but does not provide the operations support systems needed for interconnecting carriers to have the same access to the unbundled element as the ILEC has.
> - The interconnecting carriers complain about the compliance tariffs but one of those carriers, facing a business imperative to enter the market under any conditions, concurrently purchases an unbundled loop or perhaps a few.
> - Initially, ordering and provisioning is performed using a manual/paper process, in contrast to the electronic, real-time processing available to the ILEC itself.
> - When the ordering/provisioning process becomes totally unworkable (typically because the interconnecting carrier seeks to order more than a few loops and the ILEC cannot handle the order), the interconnecting carrier files a complaint with the state commission.
> - The State commission commences "collaborative meetings" in which the staff requests all parties to participate.
> - The ILEC uses every opportunity to turn the collaborative process into resource and time "black holes" with no firm time frame for resolution of the issues.[6]

In its Comments, Tele-Communications, Inc. (TCI) provides additional evidence of the need for

[6]Comments of MCI at 25.

effective rules and enforcement of those rules. A veteran of numerous state proceedings on local competition, TCI offers a litany of examples of barriers which it and other competitive LECs have experienced when attempting to negotiate interconnection agreements.[7]

CPI wishes to emphasize that many of these cited activities of the LECs, while anti-competitive, are probably legal. They simply constitute the exercise of tactics available to very large, monopoly incumbents. Neither are these companies necessarily venal; it is more rewarding to be a monopoly and it is natural to act to defend that status, even while rhetorically supporting competition. The lesson here is merely that these tactics are available, are used, and must be mitigated if competition is to have a realistic chance to develop.

Another informed opinion on the subject of the proper role of the FCC is the Department of Justice:

> The Department of Justice strongly endorses the Commission's declared intention (Notice ¶¶ 25-41) to play an active role in bringing about the "pro-competitive, deregulatory, national policy framework" that Congress expressed in the 1996 Act. In order to achieve the rapid and successful development of local competition, the Commission, in this rulemaking, should articulate clear, national standards governing issues that are critical to the rapid emergence of competition.
>
> Clear national standards are critical to assure that entrants will have prompt access to essential facilities or services of incumbent monopolists, on economically appropriate terms. The Act places substantial reliance on negotiations between ILECs and their potential competitors to implement the detailed requirements of interconnection and unbundling, but such issues are sufficiently complex to allow lengthy delays in negotiations; consequently, the contemplated private negotiations cannot be expected to succeed quickly in the

[7]Comments of TCI at 22.

> absence of clear national guidelines or standards. There is no basis in economic theory or practice to expect incumbent monopolists to quickly negotiate arrangements to facilitate disciplining entry by would-be competitors, absent clear legal requirements that they do so. Negotiations between incumbent monopolists and new competitors over access and interconnection have frequently been prolonged and difficult, replete with claims that the incumbent has engaged in delaying tactics, and in the end regulatory or other legal intervention has commonly been necessary to reach a satisfactory result.[8]

CPI endorses this view of the Department of Justice and agrees with DOJ that Congress intended to encourage[9] competition in local telephone markets, not merely to deregulate and watch the results of negotiations among monopolies and would-be entrants.

In our Comments, CPI argued that a strong federal role was essential to the timely development of local competition and that this outcome was critical to the welfare of consumers. We were joined by other consumer commenters in asserting that successful introduction of local exchange competition will take the dedication and resolute efforts of regulators.[10]

Consumer support for the encouragement of local competition follows from this fact: the consumers' interest is now linked to the successful introduction of local exchange competition. Consumer advocates have experienced first-hand the limits of the ability of regulation to deliver quality services at fair prices. In many cases, consumer support for competitive approaches

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[8]Comments of the Department of Justice at 9-10. Footnotes omitted.

[9]Comments of the Department of Justice at i.

[10]See, for example, Comments of the Texas Office of Public Utility Counsel.

preceded that of the Congress. Whereas a few years ago interconnection and competition were largely carrier-to-carrier issues, they are now central consumer issues as well.

III. The Commission Should Balance The Roles of the FCC and the States by Providing a Regulatory Model for States to Use In Implementing the 1996 Act. The Model Should Specify Minimum Levels Of Unbundling and Interconnection and Set Broad Pricing Standards for the States to Use in Arbitrating Interconnection Negotiations.

The appropriate balance of state and federal regulation was a central theme in the comments of many parties to this Docket. As we noted in our original comments, the goals and purposes of the 1996 Act will not be met without the coordinated efforts of state and federal regulators.

The 1996 Act makes it clear that Congress considers the development of local exchange competition to be a matter of national concern. The development of local exchange competition is key to virtually all other provisions of the legislation: entry by the RBOCs into proscribed markets, deregulation, universal service support, expanded consumers choices, etc. The broad preemption of state and local statutes or regulations which would prohibit competition, contained in §253, is strong evidence that Congress expects its action to result in the rapid introduction of local competition. Because of this strong federal view, it is untenable to believe that Congress contemplated that the FCC have only a ministerial role in the implementation of the 1996 Act. The Commission must exercise a central coordinating role, and not be constrained to backing up the states or merely regulating price of the "interstate" portion of network elements.

But neither should the 1996 Act be read in the other extreme to relegate state commissions to the

role of mere "federal agents."[11] The correct approach is easy to discern: the Commission and the States share responsibility for implementing the Act. CPI supports a regime in which the FCC, based largely on the experiences of states that have already moved forward, determines the fundamental issues (pricing and availability of interconnection and unbundled network features) that will make or break the rapid development of local competition. State commission, acting within the policy framework, implement the local competition provisions of the Act by arbitrating interconnection negotiations, imposing conditions and pricing as appropriate and required. State commissions maintain authority for ratemaking for today's jurisdictional services.

CPI respectfully disagrees with NARUC and other commenters who suggest that the Act contemplates a jurisdictional separation of network functions. As the debate over the treatment of exchange access in the legislation illustrates, the usefulness of "separations" is disappearing. CPI cannot conceive of the advantages of creating new classes of "interstate" and "intrastate" network elements. Carriers will not make the distinction, consumers will not make the distinction and there is nothing to be gained (and much to be lost) if regulators make that distinction. If consumer use of the Internet has taught us anything, it is that geographic boundaries have little meaning or application any longer in telecommunications. Notwithstanding the legal arguments advanced by state commissions in briefs in this Docket, CPI respectfully suggests that the policy preference should be for a non-jurisdictional or

[11]Comments of New York State Department of Public Service at 2.

omni-jurisdictional view of the elements.

Both the States and the FCC have an irreducible role in implementing the Act. If competition is to develop in each state and new networks developed by national carriers, surely we must give some weight to the arguments that consistency in the basic approach is desirable. We agree with the vast majority of commenters that support adoption of national rules. We recognize that national consistency may, in some cases, stifle useful experimentation. Yet there are also limits and costs associated with Justice Brandeis' "states as laboratories". The basic analysis employed here should be of the benefits and costs of two contrasting approaches. It is our considered opinion that a strong federal role in implementation best serves the interests of both competition and consumers.

Most of the ILECs have expressed a strong preference for limited federal regulatory involvement in the core decisions about local exchange competition. CPI fears that this is mere forum shopping. Since the Commission has expressed its opinion about certain basic directions these rules should take (e.g., incremental-cost-based pricing, substantial unbundling) the LECs suddenly have a new found taste for state regulation. They would like to move the debate back to their home turf where the exercise of their political power, especially in state legislatures, is relatively stronger.

Our support for national rules is not an implied criticism of state commissions. On the contrary, we recognize that it was the leadership of some states -- Illinois, New York, California,

Washington, Colorado, Maryland and others -- which made it possible for the Congress to conclude that local competition was feasible and should be made a central part of the 1996 Act. The FCC similarly owes a debt to these commissions (that acted well in advance of Congress) for showing the way to implementation of local competition. We reiterate our formula: the Commission should decided threshold issues, the States should implement the model on a state-by-state (and ILEC-by-ILEC) basis.

Finally, we note that the entire debate about the balance between federal and state roles is being conducted as if the job of regulation were static. In fact, it is not. State regulation is inexorably moving away from economic regulation of telecommunications carriers and toward two other roles: referee among competitors and guarantor of consumer rights in a competitive market. We predict that the current narrow debate about who has the jurisdiction to set the prices of unbundled network elements will be seen in diminished importance as state and federal regulators take on their new roles and as competition transforms the industry.

IV. The Commission Should Specify the Use of Total Service Long Run Incremental Costs as the Standard for Pricing Interconnection and Unbundled Network Elements

The Comments in this Docket contain ample discussion of the merits of using an incremental-cost-based approach to pricing network elements and interconnection. We will not repeat those arguments here. In our opening comments, CPI supported the Commission's tentative conclusion to base inter-carrier prices using that standard. We note that the use of TSLRIC

pricing standard was supported by a very broad spectrum of commenters, including consumers[12] new entrants[13], wireless providers[14], state regulators[15], and the Department of Justice[16].

The ILECs are in near uniform opposition to the use of TSLRIC as the standard for pricing network elements.[17] The arguments usually reflect the position that the ILECs must be able to recover their total costs of their investment (measured by accounting costs).

The Commission should reject ILEC arguments of entitlement to recovery of all historic costs from their new competitors in the local exchange market. Simply put, the ILECs must fund their response to competition from increased efficiencies, growth in telecommunications markets and re-valuation of assets in some cases. Indeed, the Commission's pricing proposal gives meaning to its vision of a competitive telecommunications market in which a competitive firm's "prowess

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[12]See, for example, Comments of Texas Office of Public Utility Counsel and Comments of CFA/CU.

[13]The opinion among new entrants concerning TSLRIC pricing for network elements appears to be unanimous in support of the standard.

[14]See Comments of Airtouch Communications at 14.

[15]Although state commissions generally opposed the Commission promulgating pricing rules, several states use TSLRIC or LRIC-based pricing standards or agree such standards are appropriate. See, for example, Comments of California, Texas, Illinois, and Florida.

[16]Comments of the Department of Justice at 27.

[17]Frontier, which advocates the use of TSLRIC pricing, was a notable exception to the ILEC position on costing for unbundled network elements. Frontier's simultaneous presence as an ILEC, CLEC, IXC and wireless provider probably accounts for its corrected vision of the future of this industry and the implications for pricing elements. See Frontier Comments at 20.

in satisfying consumer demand will determine its success or failure in the marketplace."[18] It is time for regulators and regulated companies to break with the past comforts of revenue requirements regulation and give meaning to that vision.

Passage of the Communications Act of 1996 reprensented a fundamental realigment of equities among telecommunications providers. It is inconceivable that the massive change could have left any carrier (ILEC or CLEC) with the same expectations of its future. Because the incumbent LECs will have access to new telecommunications and cable markets, they will be able to share in the industry's growth in a fundamentally different manner than permitted before passage of the 1996 Act. We understand that ILECs will probably assert this claim for historic cost recovery over and over again before state commissions. For this reason, it is imperative that the Commission stay the course and adopt a competition policy which will bring competitors into the local exchange markets, blocking the ILECs' ability to charge rates higher than reasonable economic costs.

LCI International notes the difficulty in arriving at precise TSLRIC-based price ceilings and suggests that the FCC refer the specification of TSLRIC-based prices to a Federal-State Joint Board.[19] Under LCI's proposal, the Joint Board would act to establish ceiling prices applicable to interconnection rates and network elements. We recognize the short timeframe within which

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[18]CC Docket 96-98, Notice at ¶1.

[19]Comments of LCI International at 6.

such a Joint Board consideration must occur. Nevertheless, this is a reasonable proposal which deserves careful consideration by the Commission.

V. Bill and Keep Arrangements May Produce Efficient Inter-Carrier Transactions and Should Be Available to the States to Impose in Arbitration

CPI supports the use of TSLRIC pricing for traffic termination. However, as we noted in our initial comments, there are known impediments to this regime, including the cost and ability to measure terminating local traffic. Further, given assumptions about traffic between LECs and the relative costs of efficient LECs, the economic and engineering precision gained by measuring traffic and establishing TSLRIC rates for each LEC to use in billing may not be worth the cost.

In our initial comments, we suggested that mutual traffic exchange ("bill and keep") was potentially a very useful method for compensation of costs of traffic termination. We were pleased that a number of parties also endorsed bill and keep as a feasible and practical method, at least in an interim period, to facilitate an early start to local exchange competition.

We agree with the analysis of the Department of Justice:

> The Commission should also consider, however, the possible advantages of bill and keep arrangements as an interim -- and perhaps permanent -- standard for pricing transport and termination.
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> * * *
>
> The Department does not believe that, in the short term, bill and keep would have a deleterious effect on competition or the incumbent telecommunications carriers, and has clear advantages of being an easily determined and administrable

> standard. There appears to be ample evidence that bill and keep is being used successfully between telecommunications carriers today. In particular, these arrangements are used by neighboring LECs to exchange traffic.[20]

We also agree with the analysis provided by TCI, including the observation that any inaccuracy resulting from bill and keep will have a less destructive effect on competition than inaccuracy resulting from a positive price for interconnection, transport and termination. TCI concludes correctly that bill and keep will likely permit competition to develop sooner that other interim pricing approaches.[21] The Association for Local Telecommunications Services (ALTS) offers a cogent argument for why competitive LECs should, at their election, have a right to bill and keep arrangements.[22] Part of ALTS' arguments echo the analysis of the Department of Justice that the marginal cost of traffic termination in offpeak periods of the day is near zero.[23]

Although local exchange carriers have traditionally used bill and keep arrangements between neighboring (non-competing) LECs, most ILECs now oppose bill and keep as a method for pricing traffic termination with competing carriers. The United States Telephone Association opined that the mandatory use of bill and keep constitutes a taking and violates the Fifth Amendment to the Constitution.[24] USTA's analysis relies the claim that "[b]ill and keep

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[20]Comments of the Department of Justice at 34.

[21]Comments of TCI at 37.

[22]Comments of ALTS at 43

[23]Comments of the Department of Justice at 34.

[24]Comments of USTA at 84.

arrangements permit no cost recovery from the originating carrier." [25] But USTA neglects to mention that the terminating carrier in its example, whose property is allegedly being taken, may well be a net gainer under a bill and keep arrangement, avoiding more costs than it expends. In any event, the ability to terminate traffic on other networks without cost certainly offsets the requirement to terminate traffic from other carriers. The question is an empirical one and should be analyzed accordingly.

Having considered the comments of other parties in this Docket, we remain convinced that the Commission should adopt rules that permit States to impose bill and keep arrangements, at least on an interim basis, to effectuate the rapid growth in local exchange competition. We would also agree that States should consider whether traffic imbalances in some circumstances could imperil the fairness of bill and keep systems.

VI. An Arbitrated Interconnection Agreement Should Be Binding on the Parties Unless Parties Mutually Agree to Amendments; The States' Role in Arbitrating Interconnection Agreements Should Not Be Limited by "Baseball"-Style Arbitration Rules

In its Comments, SBC Communications, Inc. asserts that the Commission should interpret the 1996 Act to say that the decision of the State commission, following arbitration, is not binding on the parties to the arbitration. Specifically, SBC offers the following interpretation of the meaning of the 1996 Act:

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[25]Comments of USTA at 83.

> A critical point of clarification relates to the non-binding nature of arbitration decisions under the Act. The NPRM alludes to this area where it refers to an arbitrator's decisions regarding "which of the two proposals becomes binding." Congress did not intend for parties to "be bound" by arbitration decisions under the Act in the sense that they are legally obligated to enter into an agreement after receipt of the arbitrator's decision. Clearly, if they decide to enter an agreement, then they must incorporate the arbitrator's decision (unless of course they decide to re-negotiate the entire agreement), but it is equally clear that they are not legally obligated to enter into any agreement at all after an arbitration decision if either party at that point does not wish to do so.
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> Congress's intent is apparent from the fact that parties must subsequently submit signed agreements to state commissions for separate review after an arbitration decision. Congress could have provided that, after the state's arbitration decision, the state then automatically reviews the remainder of the agreement for overall approval under Section 252(e), but it did not do so. Rather, it provided for a second, separate submission to the state commission of the parties' agreement in its entirety, with a second review period. This indicates Congressional intent that arbitration decisions not compel parties to enter into an agreement if one or the other still objects after an arbitration case.

This is, to say the least, a shocking interpretation of a central provision of the 1996 Act. Assuming this opinion represents SBC's legal position going into interconnection negotiations, it appears that a new entrant must abandon all hope when entering into negotiations with SBC; following negotiations and arbitration, SBC may walk away from a result it does not like.

But SBC has also advanced an illogical interpretation of the 1996 Act that makes a mockery of state regulation. It is hard to imagine what Congress had in mind when it constructed the negotiation/arbitration process if either party could simply reject the arbitrator's decision. It is also difficult to rationalize why Congress would have created a "duty" to provide interconnection for incumbent LECs, only to have that duty undermined by the LEC's unilateral ability to stonewall in negotiations and then ignore the opinion of an arbitrator. Finally, it is cynical of

SBC to suggest that a state regulator's ruling is merely "advisory" and without effect if one of the parties chooses not to accept it. SBC's "Heads-I-Win, Tails-We-Don't-Play" attitude could have grown up nowhere else except within a monopoly.

To evaluate the effect of SBC's striking interpretation of this provision, we must realize that interconnection negotiations between ILECs and CLECs will not be symmetric. A CLEC cannot even contemplate local exchange entry until it has secured interconnection arrangements and has agreed to a specific price for resale and the purchase of network elements. A negotiated asgrement or an arbitrated result is absolutely essential to a new entrant. On the other hand, an ILEC has little business incentive to cooperate with a CLEC during the initial interconnection negotiations. An interconnecting carrier is a competitor. All things being equal, the ILEC is better off without an agreement and without a competitor.

We acknowledge that the "carrot" of manufacturing and interLATA entry will eventually provide some incentive for an RBOC to negotiate in good faith. But this incentive operates in the longer run and does not diminish the incentive in the short run to frustrate the business plans of local exchange competitors, especially during a period when the LEC can gird for any future competition, rebalance rates and generally exercise its market power. We agree with the Comments of LDDS Worldcom that the ILECs have unequal bargaining power and that federal and state regulators must act to limit the ability of ILECs to exercise this power.[26] But the

[26]Comments of LDDS Worldcom at i.

creation of rules, at the FCC or in the States, will have no effect on this power imbalance if arbitration were given the interpretation sponsored by SBC.

SBC's interpretation of §252 is apparently not shared by all other ILECs. Ameritech describes arbitration as limiting the bargaining power of the ILEC:

> The agreement eventually reached through the arbitration process is subject to approval by the relevant state commission, and this decision of the state is, in turn, subject to judicial review in federal district court. These provisions neutralize any alleged bargaining advantage that an incumbent LEC might otherwise have had in imposing terms or delaying resolution of issues. If an incumbent LEC does not offer reasonable interconnection terms, that LEC risks having unfavorable terms imposed on it by arbitration.[27]

Unless, of course, one adopts SBC's view of arbitration. The Commission should clarify for SBC its interpretation of whether arbitration is binding on the parties.

There is, of course, a limited sense in which parties are not bound by the decision of the arbitrator. By mutual agreement, the parties to the arbitration can re-negotiate part or all of the contract. This suggests that State commissions should be prepared to offer "advisory opinions" prior to commencement of negotiations or following the joint request of the parties to a negotiation. Such opinions could help by guiding the negotiations and could be offered by the State commission as part of its role as mediator.[28]

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[27]Comments of Ameritech at 8. Footnote omitted.

[28]See 47 U.S.C. §252(b)(1).

In the Notice, the Commission enquires whether "last offer" arbitration (also known as "baseball" arbitration) might make negotiations and arbitration more efficient by raising the stakes for any party that maintains an unreasonable position in negotiation and takes that position to arbitration. The Commission raises this issue in the discussion of its possible duty to assume the role of a state which has not acted on an interconnection agreement. Several commenters, including the United States Telephone Association[29] and SBC[30], endorsed the use of final offer arbitration.

We agree that final offer arbitration could provide more expedient results. That's probably good for baseball. However, State commission or FCC arbitration of interconnection negotiations involves more than a limited dispute between two private parties. Especially at the beginning of this process of implementing the 1996 Act, States and the Commission will be dealing with contentious, new issues whose outcome has implications for the public interest.

CPI suggests that "baseball" type arbitration should not be used. First, as the Commission points out in the Notice, it is possible that neither position of the negotiators will serve the public interest. Relevant here are the Comments of the Ohio Office of Consumers' Counsel which points out that "final offer" arbitration would have to be modified to ensure that the Commission

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[29]Comments of USTA at 94.

[30]Comments of SBCCommunications at 102.

or State was able simultaneously to serve the interests of the parties and the public interest.[31] Second, the Commission or State commission should have the latitude to construct a solution which was not identical to the position of either party. In some cases, the Commission or State may wish merely to "split the difference" between the sides in dispute; in other cases a qualitatively different solution may be appropriate.

Finally, we disagree with those commenters that propose that States and the Commission close the arbitration process to all but the two parties that bring the dispute forward.[32] As described above, these disputes will border on important public policy issues. Depending upon the exact format chosen by the State or the Commission, there should be opportunity for interested parties to participate, at least having the opportunity to file comments in the proceeding. CPI does not believe that a fully-litigated evidentiary hearing will be needed, especially if the negotiating parties have bargained in good faith and narrowed the differences. As a general matter, these matters can probably be handled as paper hearings if a state's administrative procedures permit. However, there is also no need for backroom deals that exclude consumer representatives and others with a bona fide interest in the outcome.

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[31]Comments of the Office of the Ohio Consumers' Counsel at 50.

[32]See Comments of USTA at 95 and Comments of SBC Communications at 104.

VII. Conclusion

The Competition Policy Institute appreciates the opportunity to provide these Reply Comments on the Commission's Interconnection Rule. Once again, we commend the Commission for its pro-competitive orientation in the Notice and recommend that the final rule incorporate the suggestions made in these Reply Comments.

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